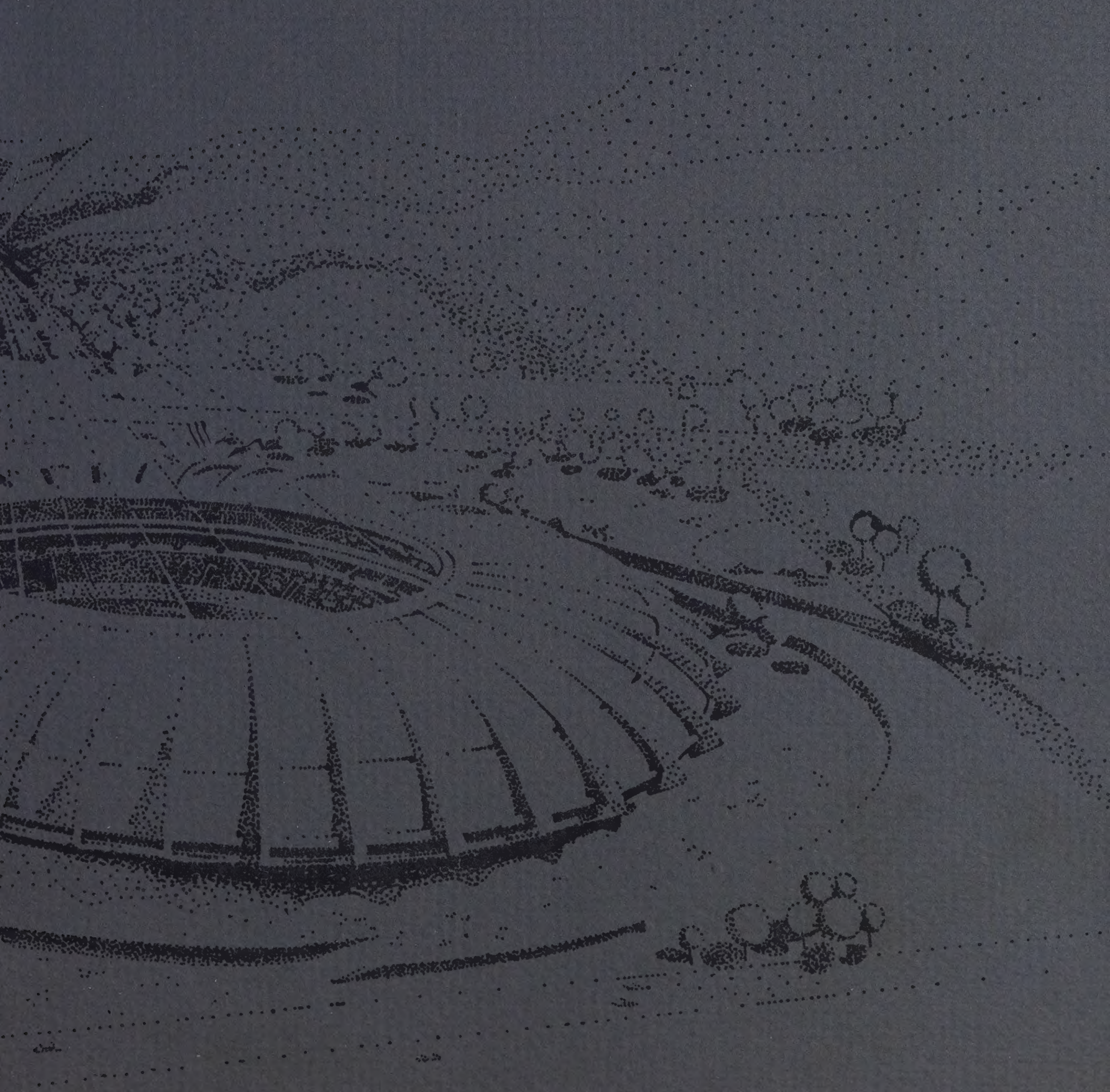
Comcorp

COMTECH
Group International Limited

1975 Annual Report



Directors

Michel Bourbonnais
J. Heath Halliday
James E. Houston
Edward K. Loyst
Donald M. McPhail
John D. Morand
Sinclair M. Stevens

Officers

Sinclair Stevens, *Chairman*
James Houston, *Vice Chairman*
Donald McPhail, *President*
Bruce Gall, *Executive Vice President*
Heath Halliday, *Vice President, Ontario*
Karl Brdlik, *Vice President, Quebec*
John Morand, *Treasurer*
Noreen Stevens, *Secretary*

Head office

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Cambridge (G), Ont.
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Reston, Virginia, U.S.A.
Area Code 703 - 471-7141

Annual general meeting

The 1975 Annual and General Meeting of Shareholders of Comtech Group International Limited will be held in the Prince Edward Island Room of the Royal York Hotel in Toronto, at 3:30 p.m. on October 16, 1975.

COMTECH

1. *Package services division*

While Comtech continues to be Canada's number one payroll processor, with over 1,000 payrolls, other computer package accounting services are contributing strongly to the company's financial growth.

An increasing number of Comtech customers are being encouraged to use more than one of these packages. Apart from payroll – the foundation on which these other packages have been built – they include job costing, accounts receivable, accounts payable, and general ledger. Strong movers this past year have been Autopay (a payroll package designed for smaller companies) and the financial products of the general ledger system.

Changes in federal government requirements, and more involved wage computations, are contributing to the growing complexity of payroll preparation. Many companies, in fact, are finding it no longer makes economic sense to process their own payrolls. They are beginning to realize that specialist computer utilities, such as Comtech, are not only better equipped to handle the payroll chore but can do it more economically than they can handle it on their own in-house systems.

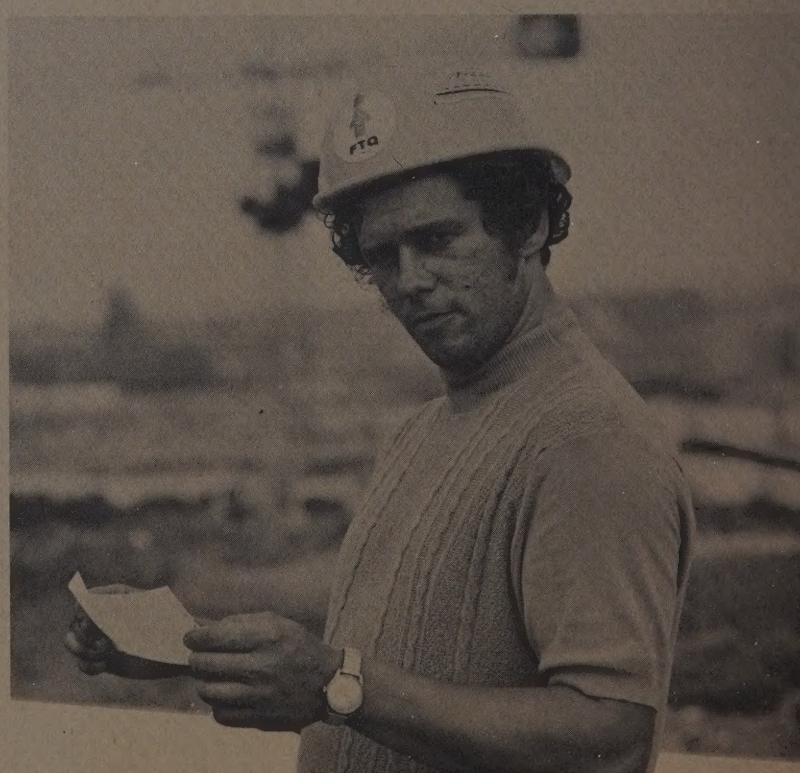
The changing computer climate has also changed people's attitude to payroll processing. At one time payroll was the first application to be put on a new computer. Today, as more and more companies begin to treat their EDP operations as cost centres, payroll is dropping lower and lower on the list of priorities. To many it's a demeaning application that is becoming increasingly difficult to justify on a cost-effective basis.

Comtech's job costing package is gaining in popularity as profit squeezes in industry make it even more important for management to maintain a tight rein over labour costs. Job costing dovetails with the payroll systems to give an in-depth analysis of just where the labour dollar is going.

Similarly, with the accounts receivable package, it's not simply a question of selling a processing service . . . Comtech is marketing a facility that enables its customers to collect money. Accounts receivable represents a company's largest reservoir of untapped funds and – particularly in these recent months of tight money conditions – a computerized package such as this is invaluable not only in speeding up collections and improving the cash flow but, generally, in assisting with credit administration.

Comtech's package services are improving in excellence each year . . . new additions are being made to the line of packages . . . and the division that markets these packages is expanding on a geographic basis.

The job of building the site for the 1976 Montreal Olympics (see cover) was mammoth; thousands of men working in many different locations at dozens of different pay scales. Pictured below is one of the construction workers. Who made sure he got the right pay cheque at the right time? Comtech.



2. *Licensing division*

"On cost, on time and it performs".

This sentence sums up the major reason for the growth in Comtech's licensed activities. Since the first license was granted to a company to use Paymaster, in 1971, Comtech has continued to sell its product software to large users who have their own in-house computers. An accounts payable and a general ledger product are recent additions to Comtech's line of licensed products.

Licensed products are successful, and able to grow, only when data processing can be provided that is more cost-effective than the same service from in-house facilities. In effect, this means that Comtech has to provide better computing with its products, and it does.

With Comtech's licensed products, management knows what it is getting and when and how much it will cost. And in tough times – when management actually needs more, rather than less, information for decision-making – users are looking for easier, less expensive and less time-consuming ways to get their computer systems running.

Computer industry estimates are that the market for package software should grow about 60 percent a year through 1977. Users realize just how viable alternative packages are to doing the same work in-house. Some estimates indicate buying a software package costs seven to 10 times less than in-house development. Because Comtech's licensed products have a fixed cost, and customers know their schedules will operate and be on time, they provide an assurance that is simply not available with an in-house program – particularly during that critical first year of operation.

All Comtech licensed products come with detailed and comprehensive documentation.

3. *On-line services division*

The Jeannie line of products, using a voice response mini-computer, is a new data processing service that Comtech offers for small and medium-sized businesses. No operator training is necessary for companies to use this interactive service whereby, using their own Touchtone telephones, companies can enter their accounts receivable, accounts payable and payroll data.

In order to ensure total accuracy the voice-response computer guides, edits, verifies and balances all incoming data. Jeannie allows companies direct access to a complete line of services and, at the same time, allows these companies both to retain control of all entries and to keep source documents on their own premises.

Comtech confidently expects on-line services to be an important growth area because they represent the type of systems that need a combination of skills many in-house DP operations do not have. Also, as a product-oriented utility, Comtech is offering small business the opportunity to run their operations with the same degree of sophistication as large organizations.

4. *Custom services division*

This division, which has a separate sales force and development group, supplements Comtech's package accounting services by providing custom programming and processing. It was formed to meet the needs of many Comtech customers who required custom packages to meet their particular requirements – specialized inventory or sales analysis, for example.

Out of this division will come Comtech's package services of the future.

Assets

	1975	1974
Current Assets:		
Cash	$ 32,017	$ 72,740
Accounts receivable	641,068	334,562
Inventories, at cost	92,212	40,420
Prepayments and sundry assets	52,476	23,455
	817,773	**471,177**
Package Programmes (Note 1)	302,234	213,134
Fixed Assets (Note 1):		
Cost	1,007,895	915,478
Accumulated depreciation	646,622	518,653
	361,273	**396,825**
Other Assets and Deferred Charges	17,250	25,496
Goodwill and Excess of Cost of Investments in Subsidiaries over Net Assets Acquired (Note 1)	820,794	595,380
	838,044	**620,876**
	$2,319,324	**$1,702,012**

Approved on behalf of the Board:

(Director)

(Director)

See accompanying notes.

Consolidated Balance Sheet – June 30, 1975

Liabilities

		1975	1974
Current Liabilities:			
Bank indebtedness (Note 2)		$ 125,000	$ 40,000
Accounts payable and accrued liabilities		271,764	221,038
Current maturities on long-term debt (Note 2)		94,500	55,106
		491,264	**316,144**
Long-Term Debt (Note 2)		108,500	–
Minority Interest		–	11,896
		599,764	**328,040**
Shareholders' Equity (Note 3)			
Capital Stock:			
Authorized:			
14,490	5% First Preference shares, $10 par value, cumulative, redeemable at $10.20 a share		
157,482	3% Second Preference shares, $1 par value, non-cumulative redeemable at par		
2,000,000	Common shares, $1 par value		
Issued:			
4,490	5% Preference shares	44,900	44,900
55,482	3% Preference shares	55,482	55,482
885,713	Common shares	885,713	885,213
		986,095	**985,595**
Contributed Surplus		101,000	101,000
Retained Earnings		632,465	287,377
		1,719,560	**1,373,972**
		$2,319,324	**$1,702,012**

Consolidated Statement of Income
Year Ended June 30, 1975

	1975	1974
Revenues	**$ 2,913,715**	**$ 1,798,614**
Costs and Expenses:		
Salaries and benefits	815,894	451,197
Computer operations	1,024,371	687,133
Marketing and administration	712,226	415,251
	2,552,491	**1,553,581**
Income before taxes and minority interest	**361,224**	**245,033**
Provision for income taxes:		
Current	182,330	97,259
Deferred	19,065	23,117
	201,395	**120,376**
Minority interest in subsidiaries' profit (loss)	**(11,847)**	**7,360**
	189,548	**127,736**
Income before extraordinary item	**171,676**	**117,297**
Extraordinary item:		
Tax reduction due to application of tax losses forward	184,637	110,009
Net Income	**$ 356,313**	**$ 227,306**
Earnings per share:		
Income before extraordinary items	.19	.13
Net income	.40	.26
Average number of shares outstanding	885,424	876,793

Consolidated Statement of Retained Earnings
Year Ended June 30, 1975

	1975	1974
Retained earnings at start of year	$ 287,377	$ 71,296
Net Income	**356,313**	**227,306**
	643,690	**298,602**
Dividends paid on 5% preference shares	11,225	11,225
Retained Earnings at End of Year	**$ 632,465**	**$ 287,377**

See accompanying notes.

Comtech Group International Limited and Subsidiaries

Consolidated Statement of Changes in Financial Position
Year Ended June 30, 1975

	1975	1974
Financial resources were provided by:		
Income before extraordinary item	$171,676	$117,297
Add (deduct) items not requiring a current outlay (receipt) of working capital:		
Depreciation of fixed assets	112,879	103,561
Amortization of deferred charges	69,628	51,901
Provision for deferred taxes and minority interest	(4,851)	2,865
Amortization of excess of cost of investments	3,200	–
Working capital provided from operations, exclusive of extraordinary item	**352,532**	**275,624**
Tax reduction due to application of tax losses forward	184,637	110,009
Increase in long term debt	108,500	–
Issue of common shares for cash	500	20,430
Miscellaneous	1,201	14
	647,370	**406,077**
Financial resources were used for:		
Acquisition of shares of subsidiary companies plus subsidiaries' working capital deficiencies at dates of acquisition	108,614	–
Purchase of fixed assets	77,327	29,116
Purchase of goodwill	120,000	–
Package programme development costs	158,728	133,364
Retirement of long-term debt	–	73,304
Payment of dividends	11,225	11,225
	475,894	**247,009**
Increase in working capital	171,476	159,068
Working capital (deficiency), beginning of year	155,033	(4,035)
Working capital, end of year	**$326,609**	**$155,033**

See accompanying notes.

Auditors' Report

To the Shareholders of
Comtech Group International Limited

We have examined the consolidated balance sheet of Comtech Group International Limited and its subsidiaries as at June 30, 1975 and the consolidated statements of income and retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at June 30, 1975 and the results of their operations and the changes in their financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Ontario,
August 28, 1975.

LAVENTHOL & HORWATH,
Chartered Accountants.

Notes to Consolidated Financial Statements

Year Ended June 30, 1975

1. Accounting policies:

The following is a summary of the major accounting policies of the company:

(i) Principles of consolidation:
The consolidated financial statements include the accounts of the company and its subsidiary companies, all of which are wholly-owned, except for Commercial Computer Services Inc. which is 99.5% owned.

(ii) Fixed assets:
The company depreciates its fixed assets on a straight-line basis over their estimated useful lives. Total depreciation during 1975 was $112,879 ($103,561 in 1974).

Fixed assets are summarized as follows:

	1975			1974
	Cost	Accumulated Depreciation	Net	Net
Computer equipment	$ 731,394	$497,262	$234,132	$306,832
Magnetic tapes	40,920	32,220	8,700	9,398
Furniture and office equipment	144,603	72,530	72,073	49,006
Leasehold improvements	90,978	44,610	46,368	31,589
	$1,007,895	**$646,622**	**$361,273**	**$396,825**

(iii) Package Programmes:
It is the company's policy to capitalize the costs of package programme development and to amortize such costs on a straight-line basis over a five year period, commencing in the six month period following incurrence of such costs.

The following is a summary of the package programmes:

	1975	1974
Balance at beginning of year	$213,134	$131,671
Package programme development costs capitalized during the year	158,728	133,364
	371,862	**265,035**
Amortization of package programmes	69,628	51,901
Balance at end of year	**$302,234**	**$213,134**

(iv) Goodwill and excess of cost of investments in subsidiaries over net assets acquired:
The excess of cost of investment in subsidiaries over equity in net assets acquired relating to those companies purchased on or before April 1, 1974 is not being amortized, since in the opinion of management it has continuing value. As required by an accounting recommendation of the Canadian Institute of Chartered Accountants, goodwill and the excess cost of investments in subsidiaries over equity in net assets acquired relating to companies purchased after April 1, 1974 is being amortized; the company is using a straight-line basis for amortization over 40 years. The amount so amortized in 1975 is $3,200.

(v) Licensing revenues:
The company has entered into contracts whereby it licenses package programmes to other entities. Revenue from such contractual arrangement take the form of either a monthly usage charge or a lump sum payment. In the latter situation the licensee is granted a perpetual lease right to the particular programme.
Revenues from contracts which generate a monthly usage charge are recorded on a monthly basis. Revenues from perpetual leases are recorded on the dates of execution of contracts, provided the lump sum price is due no later than one year after execution. Also, at the date of execution of such contracts, the company accrues an estimate of its costs to be incurred in connection with completion of the installation of the system.

2. Long-term debt:

Bank loan, evidenced by a registered debenture, bearing interest at 2% above the prime commercial lending rate, repayable $21,875 quarterly commencing September 1, 1975	$175,000
Balance due on acquisition of subsidiary without interest; repayable $3,500 semi-annually to June 30, 1979	28,000
	203,000
Current maturities	94,500
	$108,500

The above bank loan as well as the bank indebtedness of $125,000 shown as a current liability, are secured by a first fixed charge on the company's computers located in Toronto, and a general assignment of book debts. This computer equipment has been fully depreciated for accounting purposes.

The payments in each of the next five years required to meet aggregate principal retirements of the long-term indebtedness as at June 30, 1975 are as follows:

1976	$ 94,500
1977	94,500
1978	7,000
1979	7,000
1980	–
	$203,000

3. Shareholders' equity:

(i) Capital stock:
During the year the company issued 500 common shares for $500 cash, under its stock option plan.

(ii) Stock options:
Under its stock option plan, there is an option to purchase 2,000 common shares outstanding at June 30, 1975. This option is exercisable at $3.25 per share.

(iii) Retained earnings:
During the year 1972 a transfer of $117,057 was made from contributed surplus to reduce deficit.

During the year the company paid dividends of $11,225 on the 5% cumulative preference shares, which represents five years' arrears. Dividends on these preference shares have been paid to June 30, 1964. The arrears of dividends amount to $24,695 on the 4,490 shares outstanding. Since the company failed to pay more than three consecutive half yearly dividends on these preference shares and more than four consecutive half yearly dividends on the 3% non-cumulative preference shares, both classes of shares carry voting rights.

Notes to consolidated financial statements (**3** continued)

One of the subsidiary companies has unpaid cumulative preference dividends owing to minority shareholders in the amount of $7,480.

4. Acquisitions during the year:

Pursuant to purchase agreements completed in the current year, the company acquired 100% of the outstanding shares of System Modules Limited and Pica Data Services Limited, the 30% minority interest in Comtech (U.S.A.) Inc. and the operating assets of the Toronto Data Centre of Aquila (BST). These acquisitions were accounted for by the purchase method as follows:

Net assets acquired:	
At fair values	$ 40,000
At book values	(4,164)
Excess of cost of net assets at dates of acquisition over above values, attributed to goodwill	228,614
	$264,450
Consideration:	
Cash	$236,450
Amount included in long-term debt (Note 2)	28,000
	$264,450

One of the acquisition agreements provides that additional consideration is payable in the event that the business acquired achieves specified levels of volume. The amount to be paid, if any, is not determinable at the present time and is subject to maximum payments of $60,000 on September 30, 1975 and $30,000 on March 31, 1976.

The results of operations of the companies acquired during the year are included from the effective dates of acquisition.

5. Income taxes:

Certain of the "Comtech" companies have losses carried forward for tax purposes, which have not been recognized in the financial statements. These tax losses aggregate $336,788 and expire as follows:

Amount of tax losses	Available
$149,859	1976
137,859	1977
6,245	1978
6,055	1979
36,770	1980
$336,788	

6. Commitments:

The companies are committed to annual realty and equipment rentals of approximately $450,000 in 1976, $385,000 in 1977, $285,000 in 1978, $125,000 in 1979, and $23,000 thereafter until 1986. Total rent expense in 1975 was $330,000.

7. Statutory information:

The aggregate direct remuneration paid or payable by the companies to the directors and senior officers of the company was $145,696 ($113,544 in 1974).

Total interest expense for the year was $12,740, of which $4,195 was on debt initially incurred for a period in excess of one year.